

MOODY'S ASSIGNS Aaa/P-1 RATINGS TO CalPERS CREDIT ENHANCEMENT PROGRAM

First Time Issuer Rating Assigned to \$5 billion Credit Enhancement Program

New York, January 12, 2005 -- Moody's Investors Service has assigned its highest long-term issuer rating of Aaa and highest short-term rating of P-1 to the California Public Employees' Retirement System (CalPERS) in connection with the System's soon to be launched Credit Enhancement Program (CEP). The ratings address the credit quality of CalPERS and its ability and willingness to meet senior obligations in the context of its Board approved \$5.0 billion CEP. Moody's rating conclusions are based on the Retirement System's favorable funded status and the strength derived from the large base of its contributing employer and employee members, including the System's major plan sponsor, the State of California, whose General Obligation Bonds are rated A3 with a positive outlook on Moody's municipal rating scale. In addition, CalPERS' large, diversified asset base and excellent liquidity relative to operating needs and expected program commitments also sustain Moody's highest issuer ratings.

The Credit Enhancement Program represents an extension of the portfolio investment activities of CalPERS that is intended to generate incremental fee income through a zero loss underwriting standard applicable to the issuance of letters of credit and liquidity lines in support of select investment grade municipal borrowers across the U.S. Recent legislation (AB 2364) codified the ability of California's public pension plans to engage in credit enhancement activities of the type contemplated by CalPERS. Operationally, the program is team managed by investment professionals within the Investment Division of CalPERS, and more specifically, the fixed-income portfolio management unit, with strong back-office support provided by The Bank of New York acting in an agency and administrative capacity. Conservative underwriting guidelines and geographic diversification of exposures for this national program are expected to mitigate the potential risk of draws on the Retirement System's assets.

LARGE, DIVERSIFIED ASSET BASE, STRONG LIQUIDITY, AND STRONG GOVERNANCE FACTORS

CalPERS is the largest public pension fund in the United States and third largest in the world with assets totaling \$171 billion at the end of October 2004. The Retirement System benefits from a deep and diversified pool of marketable investment assets and diverse employer base. The System's liquidity profile is excellent, with average monthly cash and equivalent balances amounting to approximately \$1.7 billion, as measured over a 5 year period. Asset allocation practices in the Retirement System's investment portfolio are also well diversified and consistent with levels established by the System's Investment Policy Committee. Portfolio assets closely approximate global investment allocations which include: 65% equities, 26% or so global fixed income, including cash and equivalent balances, and 9% in real estate at the end of October 2004.

In support of its issuer credit ratings, Moody's also cites linkages between the State of California's general taxing authority and seniority of pension obligations in the state's budget structure. CalPERS is governed by an independent Board of Directors that, by State Constitution, has plenary, sole and exclusive authority over the administration, investments and actuarial services. Plenary authority to determine contribution requirements that are binding on the State was formalized when Proposition 162 amended the California State Constitution in 1992. A subsequent court case in 1997 tested and validated this issue. Employer contributions in the 2002/2003 period amounted to about \$2.1 billion, supplemented by \$1.9 billion in contributions from members.

While funded ratios vary from plan to plan within the Retirement System and range from a low of 85.1% to a high of 122.3%, CalPERS' average funded ratio of 88% is favorable relative to other public plans, and the ratio of actuarially determined assets to liabilities is expected to revert to levels at or near fully funded status over time. The market value of the Retirement System's assets have enjoyed solid growth this past year and contribution rates have been modulated to calibrate funded ratios so as to approach full funding. The entry age normal actuarial valuation method employed by CalPERS is conservative and the actuarial assumptions are also in line with other public plan assumptions. The Retirement System's 10-year compound average growth rate of 8.5% further supports the reasonability of actuarial assumptions.

CalPERS' cash-flow profile is slated to benefit from increased system contributions, in combination with positive investment earnings. These augment the Retirement System's financial capacity relative to credit enhancement activities. The ability to make payments to current benefit recipients and cover system expenses, as well as the potential payment of obligations under the Credit Enhancement Program, is consequently possible without constraining portfolio holdings. This conclusion is not expected to be affected by current policy discussions related to structural changes to the public pension retirement system.

Moody's Prime-1 rating reflects the liquidity of plan assets in support of potential credit enhancement program commitments which notionally may not exceed 3% of portfolio assets. CalPERS maintains substantial earmarked liquidity and clearly defined administrative procedures to meet potential draws on any Credit Enhancement Program commitments. Through a combination of significant free cash balances in the System's short-term investment portfolio, coupled with U.S. Treasury, agency and mortgage securities, CalPERS' liquidity profile is strong.

STRONG UNDERWRITING STANDARDS FOR CREDIT ENHANCEMENT PROGRAM

Historically low defaults coupled with high recovery rates in the municipal finance sector for rated securities support the business case for the CEP as a low-risk extension of the System's existing investment activities. All transactions, which contemplate Letters of Credit, Standby Bond or Note Purchase Agreements, and Liquidity Lines, will be extensively analyzed and obligors subject to investment grade qualification. To be considered an eligible transaction for the program, enhanced obligations will be secured by revenues from the particular entity or back-stopped by the taxing authority of the

municipality. The CEP's portfolio is expected to be national in scope and geographically diversified amongst ten primary states to proportionately reflect dispersion of exposures consistent with aggregate municipal issuance nationwide. There are also program diversification constraints that limit concentration by issuer, industry sector and limitations that distinguish between state versus local issues in favor of local municipal commitments.

Operationally, CalPERS' strategic partnership with The Bank of New York functioning as the service agent and administrator for the program provides significant back office infrastructure necessary to support a high quality program. Moody's also cites procedural elements in support of its short-term rating where draws on pension plan assets to satisfy program commitments are to be initially met by The Bank of New York, on an interim basis. Commitments in the program will be undertaken severally with other financial institutions conducting independent due diligence and Moody's views such additional participation and syndication as favorable elements of the CEP program. Also, to minimize the incentive to maximize fee income, which could lead to increased risk, no specific rate of return is targeted. Rather, the System expects strict conformity with the stated guidelines and will let market mechanisms set the pricing of credit enhancement instruments. Term to maturity of credit instruments is expected to range from about 3 years to a maximum of 12 years, with incrementally lower portfolio exposures to longer dated credits. The weighted average maturity of credit instruments is not to exceed 4.5 years.

CalPERS is a defined benefit retirement plan that was established by state law in 1932 to provide retirement benefits for state employees. Membership is divided approximately in thirds among current and retired employees of the state, schools and participating public agencies. The Retirement System presently manages pension and health benefits for more than 1.4 million California public employees, retirees, and their families. As of June 30, 2004, benefits were being provided for 1,002,067 active and inactive members and 413, 272 retirees amongst approximately 1,200 employers.